

## Internal Revenue Service

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Department of the Treasury

Washington, DC 20224

Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

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CC:CORP:BR:6

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Date:

December 20, 2011

### Legend

Distributing =

Controlled =

LP =

LLC =

State X =

Trust 1 =

Trust 2 =

Trust 3 =

Trust 4 =

Shareholder 1 =

Shareholder 2 =

Shareholder 3 =

Shareholder 4 =

Shareholder 5 =

Shareholder 6 =

Shareholder 7 =

Business 1 =

Property 1 =

Property 2 =

aa =

Year 1 =

Dear :

This letter responds to your representative's letter dated March 31, 2011, in which you requested rulings regarding certain Federal income tax consequences of a series of

proposed transactions. The information submitted in that request and in later correspondence is summarized below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process.

In particular, this office has not reviewed any information pertaining to, and has made no determination regarding, whether the proposed transaction: (i) satisfies the business purpose requirement of § 1.355-2(b) of the Income Tax Regulations; (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (see § 355(a)(1)(B) of the Internal Revenue Code (the “Code”) and § 1.355-2(d)); or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a fifty percent or greater interest in the distributing corporation or the controlled corporation (see § 355(e) and § 1.355-7).

#### SUMMARY OF FACTS

Distributing, a State X corporation, elected to be treated as a subchapter S corporation for Federal income tax purposes in Year 1. Distributing has one class of voting common stock outstanding that is held by its shareholders through various trusts. Shareholder 1 and Shareholder 2 hold their Distributing stock in Trust 1. Shareholder 3 and Shareholder 4 hold their Distributing stock in Trust 2. Shareholder 5 and Shareholder 6 hold their Distributing stock in Trust 3, and Shareholder 7 holds its Distributing stock in Trust 4.

Distributing holds aa%, (a significant amount), of the interests in LP, a State X limited partnership. LP holds Property 1 and Property 2. Distributing along with the other unrelated partners of LP created LLC, a State X limited liability company which is treated as a partnership for federal tax purposes, in anticipation of the transaction described below. The ownership of profits, losses, and capital of LP and LLC are identical.

Distributing has submitted financial information which indicates that Business 1 (as conducted by LP) had gross receipts and operating expenses representative of the active conduct of a trade or business for each of the past five years.

#### PROPOSED TRANSACTION

For what are represented as valid business reasons, Distributing proposes the following transactions (the “Proposed Transaction”):

- (i) Distributing will form Controlled.
- (ii) LP will transfer fee simple title in and to Property 1, subject to any liabilities, to LLC.
- (iii) Distributing will contribute its aa% membership interest in LLC to Controlled (the "Contribution").
- (iv) Immediately after the Contribution, Distributing will distribute all the Controlled stock to Trust 1 in exchange for all of Trust 1's Distributing stock (the "Distribution").

### REPRESENTATIONS

The taxpayer has made the following representations concerning the Proposed Transaction:

- (a) The fair market value of the Controlled stock to be received by Trust 1 will be approximately equal to the fair market value of the Distributing stock surrendered by Trust 1 in the exchange.
- (b) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee or in any capacity other than that of a Distributing shareholder.
- (c) The five years of financial information submitted concerning Business 1 is representative of its present operations, and there have been no substantial operational changes since the date of the last financial statements submitted.
- (d) Neither Business 1 nor control of an entity conducting this business will have been acquired during the five-year period ending on the date of the Distribution in a transaction in which gain or loss was recognized (or treated as recognized) in whole or in part. Throughout the five-year period ending on the date of the Distribution, Distributing will have been a principal owner of the goodwill and significant assets of Business 1. Following the Distribution, Distributing will be a principal owner of the goodwill and significant assets of its share of Business 1 and Controlled will be a principal owner of the goodwill and significant assets of its share of Business 1.
- (e) Following the transaction, Distributing and Controlled will each continue, independently and with its separate employees, if any, the active conduct of its share of all the integrated activities of the business conducted by Distributing prior to the consummation of the transaction.

- (f) The Distribution is carried out for the following corporate business purpose: to end a dispute among the shareholders of Distributing regarding the present focus, and future direction of the business of Distributing. The distribution of the stock of Controlled is motivated, in whole or substantial part, by one or more of these corporate business purposes.
- (g) The transaction is not used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both.
- (h) The Distribution is not part of a plan or series of related transactions (within the meaning of § 1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a fifty percent or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).
- (i) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing fifty percent or more of the total combined voting power of all classes of Distributing stock entitled to vote, or fifty percent or more of the total value of all classes of Distributing stock, that was acquired by purchase (as defined in §§ 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.
- (j) For purposes of § 355(d), immediately after the Distribution, no person (determined after applying § 355(d)(7)) will hold stock possessing fifty percent or more of the total combined voting power of all classes of Controlled stock entitled to vote, or fifty percent or more of the total value of all classes of Controlled stock, that was either (1) acquired by purchase (as defined in §§ 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution or (2) attributable to distributions on Distributing stock that were acquired by purchase (as defined in §§ 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.
- (k) The total adjusted basis and the fair market value of the assets transferred to Controlled by Distributing each will equal or exceed the sum of (i) the liabilities assumed (as determined under section 357(d)) by Controlled and (ii) the total amount of money and the fair market value of any other property (within the meaning of section 361(b)), if any, received by Distributing from Controlled and transferred to Distributing's creditors in connection with the reorganization. The liabilities assumed (as determined under section 357(d)) by Controlled in the transaction will have been incurred in the ordinary course of business and will be associated with the assets being transferred.

- (l) The total fair market value of the assets transferred to Controlled in the transaction will exceed the sum of (i) the amount of any liabilities assumed (within the meaning of section 357(d)) by Controlled in the exchange, (ii) the amount of any liabilities owed to Controlled by Distributing that are discharged or extinguished in connection with the exchange, and (iii) the amount of cash and the fair market value of any other property (other than stock and securities permitted to be received under section 361(a) without the recognition of gain) received by the Distributing in the Contribution. The fair market value of the assets of Controlled will exceed the amount of its liabilities immediately after the exchange.
- (m) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.
- (n) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to the Distribution, other than intercompany loans or obligations that have arisen, or will arise, between the parties in the ordinary course of business.
- (o) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (p) No two parties to the transaction are investment companies as defined in §§ 368(a)(2)(F)(iii) and (iv).
- (q) Immediately after the transaction (as defined in § 355(g)(4)), neither Distributing nor Controlled will be a disqualified investment corporation (within the meaning of § 355(g)(2)).
- (r) Distributing is an S corporation (within the meaning of § 1361(a)). Controlled will elect to be an S corporation pursuant to § 1362(a) on the first available date after the distribution and there is no plan or intent to revoke or otherwise terminate the S corporation election of either Distributing or Controlled.
- (s) Trust 1, Trust 2, Trust 3, and Trust 4 are grantor trusts under subpart E of part I of subchapter J and thus are eligible S corporation shareholders.

## RULINGS

Based solely on information submitted and the representations set forth above, we rule as follows:

- (1) The Contribution, followed by the Distribution will constitute a reorganization within the meaning of § 368(a)(1)(D). Distributing and Controlled each will be “a party to a reorganization” within the meaning of § 368(b).
- (2) No gain or loss will be recognized by Distributing upon the Contribution except that gain will be recognized to the extent that liabilities of Distributing assumed by Controlled exceed Distributing’s basis in the property transferred. Sections 361(a), 357(a) and (c); Rev. Rul. 80-323, 1980-2 C.B. 124).
- (3) No gain or loss will be recognized by Controlled on the Contribution. Section 1032(a).
- (4) The basis of each asset received by Controlled in the Contribution will equal the basis of that asset in the hands of Distributing immediately prior to its transfer. Section 362(b).
- (5) The holding period for each asset received by Controlled from Distributing will include the period during which Distributing held the asset. Section 1223(2).
- (6) No gain or loss will be recognized by Distributing on the Distribution. Section 361(c).
- (7) No gain or loss will be recognized by (and no amount will otherwise be included in the income of) Trust 1 upon receipt of Controlled stock from Distributing. Section 355(a).
- (8) Trust 1’s basis in the Controlled stock received in the Distribution will equal the basis of the Distributing stock surrendered in exchange therefor. Section 358(a)(1).
- (9) The holding period of the Controlled stock received by Trust 1 will include the holding period of the Distributing stock surrendered in exchange therefor, provided such stock was held as a capital asset on the date of the Distribution. Section 1223(1).
- (10) Proper allocation of Distributing’s earnings and profits will be made under §§ 312(h) and 1.312-10(a).
- (11) Distributing’s momentary ownership of the stock of Controlled, as part of the Contribution and Distribution will not cause Controlled to have an ineligible shareholder for any portion of its taxable year under § 1361(b)(1)(B). If Controlled otherwise meets the requirements of a small business corporation under § 1361, Controlled will be eligible to elect subchapter S status under § 1362 for its first taxable year.

- (12) The accumulated adjustments account of Distributing will be allocated between Distributing and Controlled in a manner similar to that in which earnings and profits of Distributing will be allocated under § 312(h) in accordance with § 1.1368-2.

### CAVEATS

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter. We express no opinion about the tax treatment of the Proposed Transaction under other provisions of the Code and regulations or the tax treatment of any condition existing at the time of, or effect resulting from, the Proposed Transaction that is not specifically covered by the above rulings. In particular, we express no opinion regarding:

- (i) Whether the Proposed Transaction satisfies the business purpose requirement of § 1.355-2(b);
- (ii) Whether the Proposed Transaction is used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both (see § 355(a)(1)(B) and § 1.355-2(d));
- (iii) Whether the Proposed Transaction is part of a plan (or series of related transactions) under § 355(e)(2)(A)(ii);
- (iv) Whether Distributing or Controlled is eligible to be an S corporation;
- (v) Whether the Trusts' are eligible S corporation shareholders;
- (vi) The application of § 357(c) to the Proposed Transaction;
- (vii) The federal tax consequences under Subchapter K of any aspect of LP's transfer of Property 1 to LLC, which include but are not limited to the application of §§ 707, 731, 732, 751 and 752;
- (viii) The federal tax consequences under Subchapter K of any aspect of the Contribution, which include but is not limited to the application of § 752 (see Rev. Rul. 80-323, 1980-2 C.B. 124); and
- (ix) The federal tax consequences under Subchapter K if Controlled and Distributing are not related under § 1.752-4 when there is divergent ownership in Distributing



and Controlled following the Distribution, which include but are not limited to the application of §§ 707, 731, 732, 751 and 752.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Temporary or final regulations pertaining to one or more of the issues addressed in this ruling have not yet been adopted. Therefore, this ruling will be modified or revoked by the adoption of temporary or final regulations, to the extent the regulations are inconsistent with any conclusion in the letter ruling. See section 11.04 of Rev. Proc. 2011-1, 2011-1 I.R.B. 1, 50. However, when the criteria in section 11.06 of Rev. Proc. 2011-1, 2010-1 I.R.B. 1, 50 are satisfied, a ruling is not revoked or modified retroactively except in rare or unusual circumstances.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representatives.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

Sincerely,

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Alfred C. Bishop, Jr.  
Branch Chief, Branch 6  
(Corporate)